Legislation Boosts Farm Assistance to Highest Level Since 1993

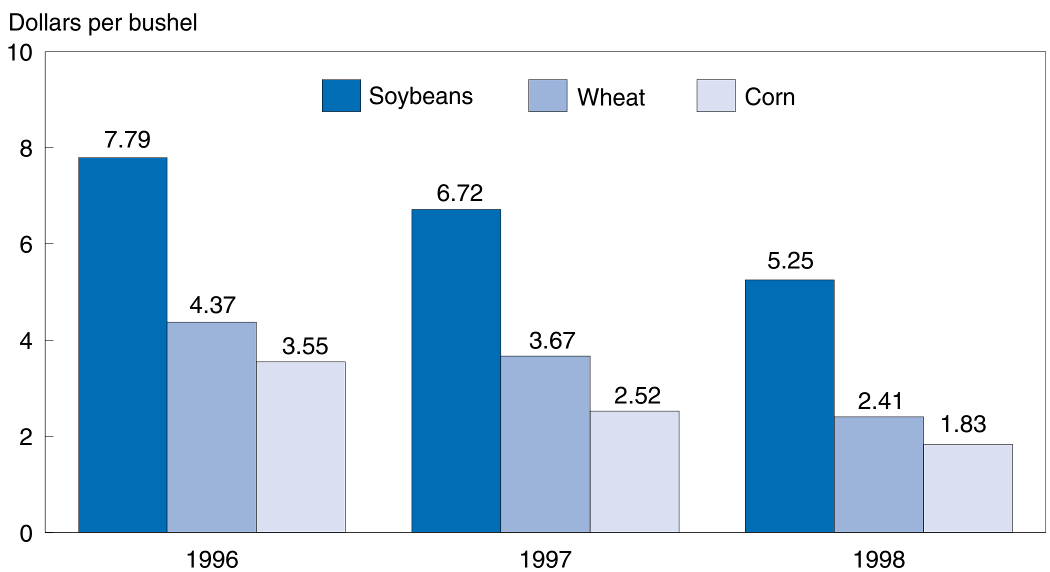
In 1996, legislation overhauled many farm programs and policies that in one form or another had been in place since the 1930's, moving the agricultural sector further toward a more market-based system. In response to financial problems faced by some producers, Congress has appropriated funding that brings the 1999 level of government agricultural payments to the highest in the decade.

The Federal Agriculture Improvement and Reform Act of 1996 (1996 Act) revised many farm commodity programs and policies, some of which had been in place in various forms since the 1930's, putting agriculture on a more market-based footing. The legislation freed farmers from most production restrictions and ended acreage reduction (set-aside) requirements. Farmers who signed up for production flexibility contracts were set to receive seven fixed, but declining, payments through 2002. This program, called the Production Flexibility Contract (PFC) program, reflected the transition from government subsidies and production controls to reliance on farm commodity prices that are largely determined by the market.

Almost 99 percent of the Nation's eligible acreage was enrolled in the PFC program. Contract commodities included wheat, corn, grain sorghum, barley, oats, upland cotton, and rice. The contract requires producers to comply with existing conservation plans for the farm, wetland provisions, and planting flexibility provisions, as well as to keep the land in agricultural use. Except for some limitations on fruits and vegetables, any commodity or crop could be planted on contract farm acreage without a loss in payments.

In 1998, a weakened trade situation due to flagging export demand, good yields in other countries, and 3 years of bumper crops in the United States, caused prices of some commodities to drop. Grain producers, particularly wheat farmers in the Northern Plains, have been among those hurt by the lower prices (fig. 1). In the midst of falling prices, unfavorable weather and crop disease aggravated the situation in 1998. While farmers in the Northern Plains had to deal with diseased crops, farmers in the South, particularly cotton farmers, had to deal with droughts, hurricanes, and flooding. Despite these yield losses, world stocks of grain and oil crops remain relatively high. Prices received by farmers fell, causing cash receipts to decline over $10 billion in 1998. This contributed to

Figure 1
September crop prices, 1996-98
Harvest crop prices on the decline since 1996



Source: National Agricultural Statistics Service, USDA.

the $2.8 billion decline in net farm income in 1998 (fig. 2), which would have been a larger decline were it not for the emergency farm assistance.

With the 1996 Act's production flexibility payments, farmers would have received declining payments from 1997 through year 2002. The payments for 1998 and 1999 were to be lower than the 1997 payments, but still higher than payments were in 1996. But, in 1998, in response to the financial problems faced by some producers, Congress substantially increased direct government payments to farmers. Congress allocated new funding through the emergency and market loss provisions of the 1998 appropriations bill. In addition, lower prices triggered provisions of the marketing loan legislation in the 1996 Act, and expanded loan deficiency payments for crop year 1998. These and other new provisions could make the 1999 level of government payments the highest in the decade of the 1990's (fig. 3).

The 1998 legislation also changed the rules so that farmers, particularly those in areas affected most by climatic disasters and lower prices for grains and soybeans, could take their entire fiscal year 1999 PFC payment in 1998. This brought 1998 production flexibility payments up to about $6 billion.

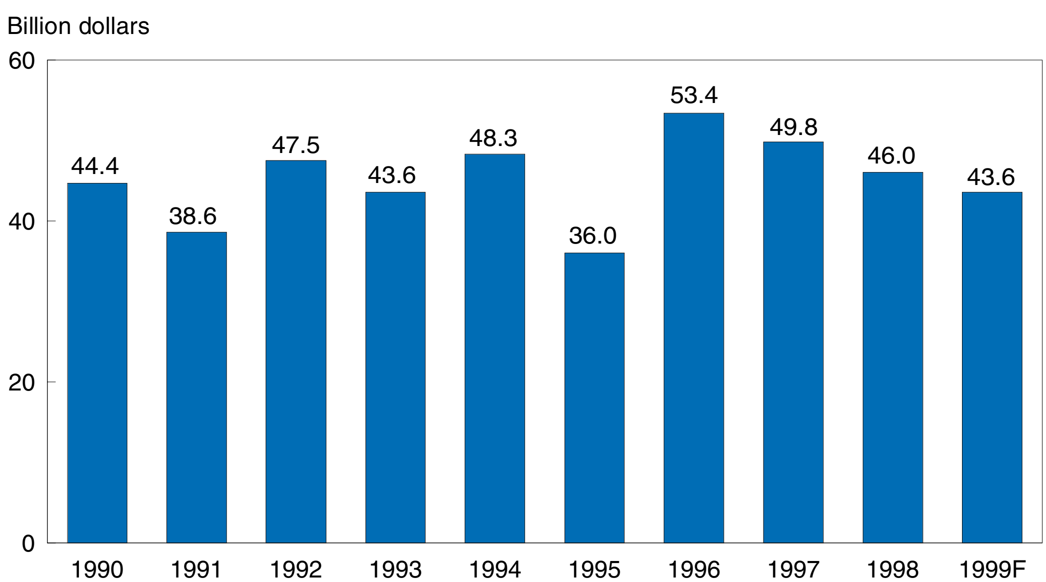
Almost $6 billion of new funding for the agricultural sector was slated for 1998-99, with disaster payments composing almost one-half of the additional funding. Farmers are receiving the disaster component during this 1999 calendar year.

Because of low prices, loan deficiency payments have become a significant portion of direct government payments in 1998 and 1999. Farmers can receive payments for the difference between the loan rate (for example, $1.89 per bushel for corn in 1998), adjusted to local markets (at the county level), and the daily market price, also adjusted to the local market. Once farmers take a loan deficiency payment for an eligible commodity, they can no longer place this same crop under a nonrecourse loan. Such payments are exceedingly complex to forecast. USDA's Farm Service Agency reported $1.8 billion in crop year 1998 loan deficiency payments. ERS's estimate was that loan deficiency payments could reach $4.5 billion in 1999. Adding the expected impact of new legislation

Figure 2

Net farm income, 1990-99

Farm income has been on the decline recently

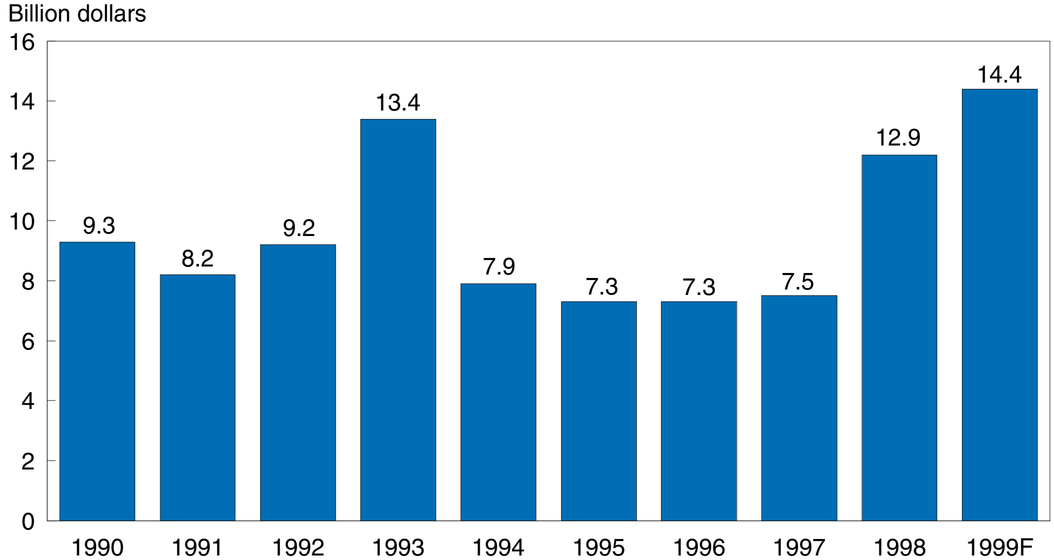


Note: F=Forecast.
Source: Economic Research Service, based on data from National Agricultural Statistics Service, USDA.

Figure 3

Government agricultural assistance payments, 1990-99

Agricultural payments have increased significantly since 1997



Note: F=Forecast.
Source: Economic Research Service, based on data from National Agricultural Statistics Service, USDA.

and the growing importance of loan deficiency payments brings the 1998 forecast of government payments to $12.2 billion and $14.4 billion in 1999.

Government Payments Important to Midwest and Northern Plains

Commodity programs were originally designed to control the supply of selected crops and support and stabilize the incomes of farmers growing those crops. For a picture of the farms and areas of the country that are most affected by government payments, we use historic data from the Agricultural Research Management Study (ARMS). (See appendix for a description of the data source.)

Billions of additional dollars from government payments will boost total farm income, but for the individual farm the importance of benefits varies widely. Not every farmer is eligible for the programs because the commodity programs were traditionally centered around crops, not livestock. Disaster programs have targeted livestock operations in the past, and the 1998 fall legislation included an appropriation for just over $400 million in livestock disaster and market loss assistance. Only about three-quarters of a million farms, or 36 percent of farms, received government payments in 1997, for an average payment of $2,903 (table 1). The participation rate in the production flexibility contract program is 29 percent of all farms.

Not surprisingly, because production flexibility payments are based on past production, larger farms received higher payments per farm. Farms with sales over $250,000 were much more likely to participate in the programs, with 55 to 70 percent of farms in this group receiving payments in 1997. These larger farms received 36 percent of payments, and produced 47 percent of program commodity sales. While the average payment for the larger farms was considerably higher than for smaller farms, payments were a smaller proportion of their gross cash income—about 3-6 percent compared with 9-12 percent for smaller farms. Limited-resource farms had the lowest rate of participation (12 percent) in the program. For this group, production flexibility contract payments averaged 9 percent of gross cash income.

Table 1

Government payments by type of farm, 1997

Very large farms get largest payments; limited-resource farms get smallest payments

Type of farm	Number of farms	Average payment	Share of farms receiving payments	Average payment for farms receiving payments
	Number	Dollars	Percent	Dollars
Limited-resource	195,572	424	19.4	2,183
Retirement	304,293	1,906	29.8	6,395
Residential/lifestyle	811,752	941	24.5	3,844
Farming occupation low sales	396,698	2,307	46.6	4,948
Farming occupation high sales	178,210	7,987	73.4	10,889
Large family farms	79,240	13,483	75.9	17,766
Very large family farms	49,804	19,411	60.5	32,087
Nonfamily	37,816	5,975	36.4	16,401
All farms	2,049,384	2,903	36.3	7,987

Note: Farm types are explained in the appendix. Government payments include production flexibility contract payments, disaster payments, payments from participation in conservation programs, EQIP cost-share payments, and payments from other State programs.

Source: Economic Research Service, based on data from the National Agricultural Statistics Service, USDA.

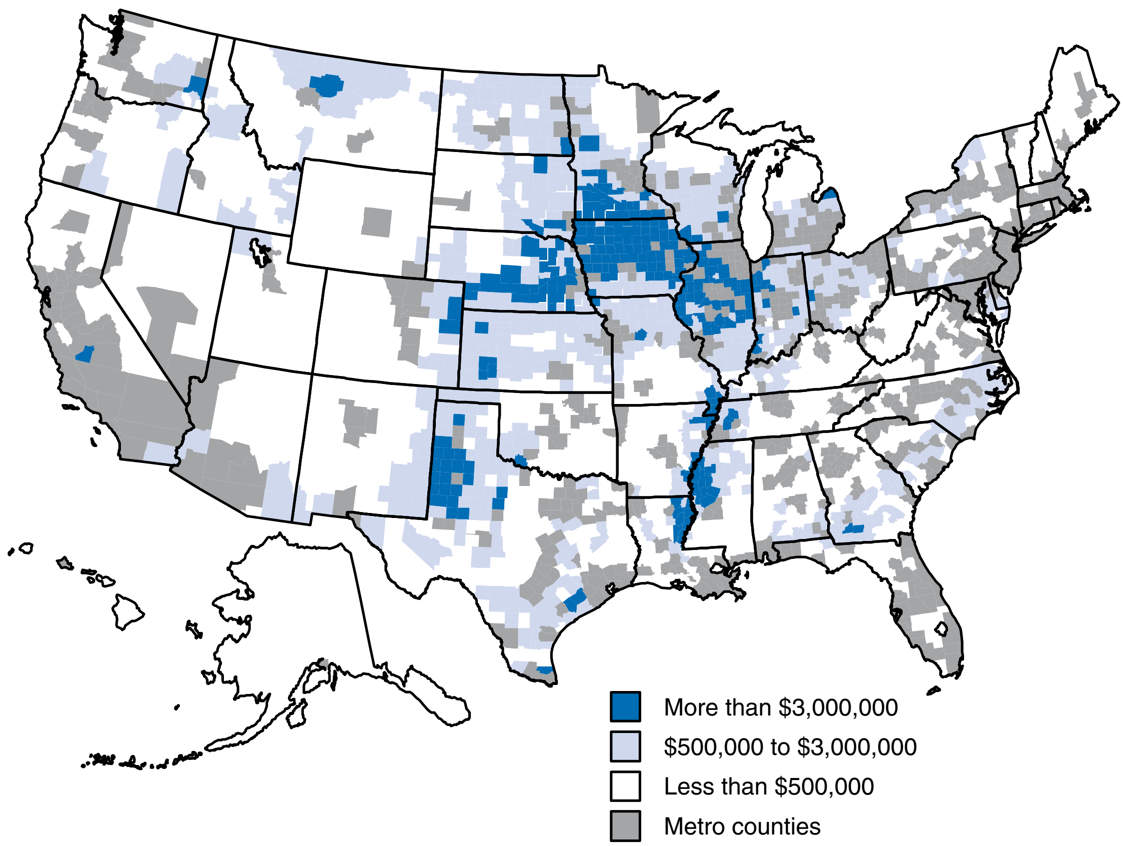
Government payments, especially from conservation programs, are particularly important for small farms categorized as limited-resource, retirement, or residential/lifestyle. These three groups make up 64 percent of the farms receiving payments from the Conservation Reserve Program or Wetlands Reserve Program. Many small farm operators report that they are retired. These operators, mainly on limited-resource or retirement farms, also rely heavily on Social Security and other public programs. Retirement farms received an average of $5,000, the highest average payment among the various farm categories under these conservation programs. Even so, operators of smaller farms depend more on off-farm wages or self-employment earnings for most of their income. Few of these farm households are affected greatly by changes in farm sector income.

How do farm program payments affect the financial viability of farms across the country? Because most PFC payments go to producers of cash grains, payments are concentrated in the Corn Belt and Northern Plains regions (fig. 4). Particularly in the Northern Plains, farms are more financially vulnerable, and are more likely to benefit from increases in income. Nevertheless, farmers in this region are more likely to have reached their maximum debt levels given current income, removing the option of taking on more debt to get through tough times. Farms in the cotton-producing areas of the Southwest also continued to have a high ratio of contract payments to gross cash farm income and high debt-to-asset ratios in 1997. Vulnerable farms (those with high debt and negative income) received about 5 percent of total government payments in 1997—roughly equivalent to

Figure 4

Direct government payments to farmers in nonmetro counties, fiscal year 1997

Direct government payments for wheat, feed grains, cotton, rice, and wool provided more than $3 million to 241 nonmetro counties, primarily in the Corn Belt, the Plains, and the lower Mississippi Valley



Note: The National Wool Act expired as of December 31, 1995.
Source: Calculated by ERS using Federal Funds data from the Bureau of the Census.

their contribution to commodity sales. Financially stressed farmers for whom payments are a large share of gross income may have some difficult adjustments ahead.

Producers who specialize in grain and soybeans have recently experienced the difficult financial situations. Their net income may fall 20 percent or more in 1999. Most grain and soybean producers operate relatively small farms (with gross sales between $100,000 and $250,000) that have much tighter cost-revenue margins than their larger counterparts. They also depend less on off-farm income than do other farm households. Because of the regional concentration of grain and soybean producers, net income reductions could be largest in the Northern Plains, Corn Belt, and Lake States. Many affected farmers may have begun 1999 by eliminating or reducing unnecessary expenditures and liquidating inventories and other assets. Increasing earning in the off-farm sector and tapping into savings are ways to offset some farm losses. When these measures fall short, producers with current debt obligations will visit their lenders to restructure existing loans and take advantage of low interest rates. Others may consider taking on new debt.

On the other hand, many farmers entered 1999 optimistically. In large part, the viability of the farm economy is derived from the financial soundness of the balance sheet. Assets are continuing to increase in value, though at a slower rate than in recent years. Growth in farm debt is expected to level off or decline, ending 6 years of increases.

Agricultural Assistance Helps Brighten Outlook for Farm Sector

Additional government payments, coupled with lower production expenses and improved receipts for some commodities, will reduce the harmful effects of low prices for the sector. Beef cattle operations should see increased earnings based on higher prices and prospects for lower expenses this year. Hog producers that have endured the current low prices and significant industry restructuring should see some income recovery. The economic outlook is also favorable for other commodity subsectors, such as vegetables, fruits, and cotton.

In recent years, prosperity in the nonfarm economy has been an important factor in maintaining average farm household incomes. There will be no exception to this trend in 1999. Even though earnings from farming are expected to be lower, average farm household income should increase with a significant contribution from off-farm earnings.

Most, but not all, farm financial problems in 1999 will be cash-flow related as a result of low prices. These cash-flow difficulties, however, reflect different economic conditions than in the early 1980's, when agriculture last suffered a financial crisis. Then, asset values were falling and farmers carried excessive debt. The declining financial situation on farms, combined with high inflation and still higher interest rates, triggered a widespread farm financial crisis. The fragile general economy made it difficult to turn to off-farm earnings to relieve any farm financial problems. Many farm businesses went bankrupt.

Now, many farms are struggling with cash flow-difficulties due to poor weather or low commodity prices, or both. These farms may not get much relief in the form of higher commodity prices in 1999. Overall, prospects for the sector are fairly good, but there will be pockets of farm stress due to the inevitable unfavorable weather and relatively low prices for some commodities. *[Janet Perry, 202-694-5583, jperry@econ.ag.gov; Mitch Morehart. 202-694-5581, morehart@econ.ag.gov; David Peacock, 202-694-5582, dpeacock@econ.ag.gov]*